

Examination Warrant Number 16-00000-76325-T1

**Report of Limited-Scope Examination of
Senior Health Insurance Company of Pennsylvania
Harrisburg, Pennsylvania
As of December 31, 2016**

For Informational Purposes Only

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Harrisburg, Pennsylvania
November 15, 2017

Honorable Joseph DiMemmo, CPA
Deputy Insurance Commissioner
Commonwealth of Pennsylvania
Insurance Department
Harrisburg, Pennsylvania

Dear Sir:

In accordance with instructions contained in Examination Warrant Number 16-00000-76325-T1, dated January 25, 2017, a limited-scope examination was made of

Senior Health Insurance Company of Pennsylvania, NAIC Code: 76325

a Pennsylvania domiciled multi-state stock life insurance company, hereinafter referred to as the “Company” or “SHIP”. The Company provides group and individual long-term care coverage. The examination was conducted primarily at the offices of the Pennsylvania Insurance Department (“Department”) located in Harrisburg, Pennsylvania and the Philadelphia offices of Oliver Wyman Actuarial Consulting, Inc.

The Company entered runoff in 2003 and is not currently writing any new business. However, the Company continues to renew business and service existing policyholders as it runs off its long-term care book of business.

The last full-scope examination of the Company was conducted by the Department as of December 31, 2013. In that examination, the Department used the services of an independent consulting firm to provide an actuarial evaluation in support of reviewing the Company’s carried reserves. Although no material deficiencies were identified in the reported actuarial reserves and related actuarial values in that prior examination, the Company reported negative income and a reduction to unassigned funds (surplus) for each year during the examination period.

The Company continued to report adverse reserve development subsequently in each of the years 2015 and 2016. Also, the Company reported material drops in statutory surplus from \$98.2 million as of December 31, 2013 to \$20.5 million as of December 31, 2016. Finally, the Department became aware of several changes in the senior officers of the Company during 2016, which could have also contributed to the deteriorating financial results.

The Department initiated this limited-scope examination with the assistance of a consulting actuary to examine the adequacy of the claim reserves and active life reserves reported by the Company as of December 31, 2016.

As this examination is limited in scope, this examination report is not intended to communicate all matters of importance for an understanding of the Company’s financial condition. The format of this report is consistent with the current practices of the Department and the examination format prescribed by the National Association of Insurance Commissioners.

This report is limited to a brief description of the Company, a discussion of financial items that are of specific regulatory concern, and a factual disclosure of other significant regulatory information related to the active life reserves and claim reserves. The Report of

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Examination of the Company as of December 31, 2013, dated May 7, 2015, should be referred to for additional historical and background information.

A report of this limited-scope examination is hereby respectfully submitted.

SCOPE OF EXAMINATION

The Department has performed a limited-scope examination evaluating reserves and related experience through December 31, 2016.

Allen J. Schmitz, FSA, MAAA, Principal and Consulting Actuary of Milliman, Inc. has served as the appointed actuary for the Company since 2015. Mr. Schmitz prepared the Actuarial Opinions and Memoranda, Valuation Filings and Cash Flow Testing for the Company.

The Department engaged the assistance of an external consultant, Oliver Wyman Actuarial Consulting, Inc. ("OW"). Marc Lambright, FSA, MAAA, of OW was the primary actuary performing the analysis, referred to as "Consulting Actuary".

The Consulting Actuary performed the following procedures:

- a. Review of experience analysis by block of business including mortality, lapse, behavior, and data related to exercising non-forfeiture options, claim incidence, claim terminations/duration, investment performance, etc.
- b. Review of historical rate increase activity and the impact of this activity on policyholder behavior and experience, along with anticipated rate actions and the expected impact of these actions.
- c. Review of claim reserve and liability assumptions and calculations, along with their consistency with SHIP actual and expected experience. This included disabled life reserves and IBNR, including provisions for any necessary claims adjustment expenses.
- d. Review of active life reserve assumptions and calculations for consistency with SHIP actual and expected experience.
- e. Review of Milliman's Actuarial Opinions and Memoranda on reserves, and supporting workpapers and documents.
- f. Review of Gross Premium Valuation projections and assumptions.
- g. Review of Cash Flow Testing projections and assumptions.
- h. Review of Department correspondence with SHIP and its external consultants to understand previously identified areas of concern, permitted practices, prior regulatory findings, etc., with a focus on work done to assess the returns, risks, and timing of cash flows associated with the investment portfolio, and an analysis of the 2016 reinsurance transaction.
- i. Discussions with SHIP and Department personnel to clarify/understand significant items related to the document review.

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The Department and the Consulting Actuary participated in numerous discussions and a review meeting was held with senior management of the Company.

FINDINGS AND RECOMMENDATIONS

The Company reported aggregate reserves for accident and health contracts of \$1,296,352,123, and a contract claims liability of \$20,791,207 on its December 31, 2016 Annual Statement.

The Consulting Actuary documented their findings, conclusions and recommendations in a report to the Department issued October 11, 2017. The Consulting Actuary report included the recommendation of an OW “base” reserve scenario and alternative scenarios, each of which indicated more adverse results than SHIP’s base scenario.

Specifically, OW found that:

1. Many of the cash flow testing assumptions underlying the asset adequacy analysis appear to be optimistic relative to recent experience, even if they are consistent with experience over a longer time horizon.
2. Claim reserves have been inadequate over the past several years and the claim reserves as of December 31, 2016 do not appear to have been strengthened substantially.
3. The Company may not obtain across all states the rate increases assumed in the internal cash flow testing model.

The Department reviewed and accepted the work of the Consulting Actuary. Upon the Department’s acceptance, the detailed findings were presented to and discussed with Company management, certain Board members and their actuarial consultants in a meeting led by the Department and the Consulting Actuary. The Company noted some disagreements with the conclusions from the Consulting Actuary, but recognized that because actuarial practice involves the estimation of uncertain events, there will often be a range of reasonable methods and assumptions.

SUBSEQUENT EVENTS

Barry L. Staldine was appointed by SHIP’s Board of Directors to be President and Chief Executive Officer of the Company, effective April 1, 2017.

Ginger Darrough, Chief Analytics Officer of the Company, starting functioning as the Company’s interim Chief Financial Officer, replacing Paul Lorentz in 2017. In early November of 2017, Ms. Darrough was appointed Chief Financial Officer by SHIP’s Board of Directors.

The Company’s reported statutory surplus declined from \$20,523,182 at December 31, 2016, to \$18,008,677 on its September 30, 2017 quarterly financial statement. The Department observes this is an approximate \$2.5 million additional decrease in surplus.

CONCLUSION

Although each of the Consulting Actuary's scenarios produce less favorable results than the Company's base scenario, and indicate material reserve deficiencies, the Department is making no recommendation to change the financial statement at this time.

The Company has agreed to consider several long-term monitoring suggestions from the Consulting Actuary and incorporate those monitoring suggestions as needed into future reserve studies. The Department will continue to closely monitor the Company's financial condition and operating results.

The next regularly scheduled financial condition examination of the Company will cover the five-year period ending December 31, 2018.

This examination was managed by Philip Judge, CFE, with actuarial support provided primarily by Marc Lambright, FSA, MAAA.

Respectfully,



Melissa L. Greiner

Director

Bureau of Financial Examinations



Philip M. Judge, CFE

Examination Manager